

October 19, 2001

**To the Honorable Mayor and Members of the City Council
City of Durham, North Carolina**

The Comprehensive Annual Financial Report (CAFR) of the City of Durham (City) for the fiscal year ended June 30, 2001 (FY 2000-01) is hereby submitted. As required by North Carolina General Statutes (NCGS), the CAFR includes financial statements that have been audited by an independent certified public accounting firm. Responsibility for the accuracy of the data, and the completeness and fairness of the presentation, including all disclosures, rests with the City. To the best of our knowledge and belief, the enclosed data accurately presents the financial position and the results of operations of the City as measured by the financial activity of its various funds. All disclosures necessary to enable the reader to gain an understanding of the City's financial activities have been included.

The CAFR is presented in four sections: Introduction, Financial, Statistical, and Single Audit. The Introductory Section includes this letter of transmittal, an organization chart and a copy of the Certificate of Achievement for Excellence in Financial Reporting. The Financial Section contains the Independent Auditors' Reports, combined statements, notes to the financial statements and more detailed combining and individual fund statements and schedules. The Statistical Section provides selected financial and general information. The Single Audit Section includes the Independent Auditors' Reports on internal controls and compliance with laws and regulations, and a schedule of expenditures of federal and state awards. This section has been prepared in accordance with the provisions of the Single Audit Act, U.S. Office of Management and Budget Circular A-133 and NCGS 159-34.

The financial reporting entity includes all of the City's funds and account groups. Component units are legally separate entities for which the City has financial control. Financial control by or dependence on the City is determined on the basis of budget adoption, taxing power, outstanding debt secured by the revenues or general obligation of the City or the obligation of the City to finance any deficits or receipt of significant subsidies from the City. Based on these criteria the City does not have any discretely presented component units. Blended component units are legally separate entities; however, in substance, their operations are included as part of the primary government.

ECONOMIC CONDITION AND OUTLOOK

Regional Picture: The Raleigh-Durham-Chapel Hill Metropolitan Statistical Area (MSA) has one of the strongest, most stable economies in the nation. In 1995 through 1998, the Raleigh-Durham-Chapel Hill MSA was rated as having the best long-term economic performance of all 316 metropolitan areas in the United States; the region was ranked 3rd nationally in 1999. National magazines consistently give the region top rankings for quality of life, higher education, overall business climate, small business and entrepreneurial opportunities, business climate for women, and combining work and family life. In November of 2000, Money Magazine rated the area as the Best Place to Live in Southern Region.

Location and Accessibility: The City is located in the heart of an MSA with a population of over 1.1 million. The City borders the Research Triangle Park (RTP) on three sides. RTP, recognized internationally as a center for cutting-edge research and development, is the largest research park in the United States. RTP covers over 7,000 acres and is home to more than 140 organizations. Durham is centrally located among the major population centers of the East Coast, and is bisected by Interstates 85 and 40, which are connected by the Durham Freeway. Raleigh-Durham International Airport (RDU), located just east of the City limits, served over 9.4 million passengers and moved 125,000 tons of cargo in 2000, making it one of the fastest-growing airports in the United States. There are about 300 daily departures from RDU, which is served by 15 commercial airlines.

Employment Base in Research and Manufacturing: The City's diverse and expanding economy is rooted in electronics, health care, medical research, education and telecommunications. The "City of Medicine" is one of the nation's leading centers for biotechnology and medical research. Duke Medical School is ranked the 3rd Best Medical School in the Country and Duke Hospital is ranked 6th Best Hospital in the Country by U.S. News. Duke University and Duke Medical Center employ 21,000 people, while spin-offs from research at Duke, the University of North Carolina at Chapel Hill, and North Carolina State University have created dozens of start-up biotech firms. These companies are supported by the state-sponsored North Carolina Biotechnology Center, located in Research Triangle Park.

Ninety-five percent of the companies currently operating in Research Triangle Park are located in Durham County. RTP employs roughly 50,000 people in such leading firms as IBM, Nortel Networks, GlaxoSmithKline-Wellcome, Cisco Systems, Novartis, and Aventis. Another 50,000 people are employed at the numerous manufacturing facilities, office parks, and flex buildings located in the City just outside of RTP, complementing the research and development activities inside the Park.

Treyburn Industrial Park in northern Durham County employs 2,000 people in firms including Becton-Dickinson, Organon Technika, Cormetech, and Fruedenberg. Japanese auto parts manufacturer Aisin AW opened a \$100 million facility there in 2000. Despite the City's reputation as a center of research and development activities, Durham is one of the few areas in the country where both the size and percentage of the manufacturing workforce is increasing as well.

Unemployment in Durham has averaged 2.3% over the past five years, and has been below 5% for each of the past 20 years. These figures are well below both the national and state averages. After reaching a record-low of 1.9% in 1999, unemployment increased slightly to 2.3% in 2000.

Education and Job Training: The education and skill level of the labor force is a major factor in the desirability of the Durham area. Over 35% of Durham County adults possess at least a Bachelor's degree, compared with 20% nationally. The community college system - particularly the system's interaction and cooperation with businesses to establish training programs - is regarded as one of the best in the nation. In-migration continues to add to the work skills and brainpower needed by our growing companies.

Construction Trends: The City continues to witness strong and solid levels of private investment, with values of building permits totaling \$760 million in fiscal year 2001. Investment totaled \$878 million countywide in 2001. Downtown Durham is targeted as an area of particular strategic and symbolic importance, and has seen such recent successes as the 250-unit West Village apartments (a renovation of historic tobacco industry buildings), the Durham Bulls Athletic Park, renovation of the 1904 TeerMark office building, and the fully leased, 90,000 square foot Diamond View office building. Other adaptive re-use successes downtown include the CityPlace offices and Measurement Incorporated's headquarters expansion. Outside of downtown Urban Retail Properties began construction of the \$220 million Streets At Southpoint Mall, which will open in March 2002.

The majority of new development in Durham County takes place within the city limits, and the City pursues an aggressive annexation policy to protect our present and future tax base.

Building Occupancy Rates: Occupancy rates in the second quarter of 2001 were 92% for flex and warehouse space, 94% for office space, and 95% for retail space. More than 3.0 million square feet of new commercial and industrial space was under development in Durham as of the second quarter of 2001. Although commercial construction has slowed somewhat in the region, reflecting a national slowdown in the economy, construction activity and preleasing rates in Durham are still strong.

Retail Sales: Fiscal year 2000-2001 retail sales in the City of Durham increased by 2.2% over the previous year. Retail sales have doubled since 1990 with an average annual growth of more than 9%.

MAJOR INITIATIVES

For the Year 2000-01

The FY 2000-01 Budget reflected the following community goals that were adopted by the City Council:

- To improve the quality of life by reducing the incidence of crime and addressing the root causes of crime.
- To improve the quality of life by ensuring the availability of, and access to, adequate, safe, and affordable housing for every resident.
- To provide economic development activities that increase citizen access to high quality jobs while increasing the City's tax base.

- To improve the livability of the City by managing the City's growth, protecting and preserving the environment, and maximizing the use of public infrastructure.
- To improve the City's image by preserving and enhancing the community's aesthetic beauty and natural assets.
- To build upon the rich and diverse cultural heritage of the community.
- To improve race relations and to preserve, enhance, and build upon the rich and diverse cultural heritage of the community.

In addition, the Administration adopted the following organizational goal:

To support the success of the community goals by maximizing the effectiveness and efficiency of the City's workforce, programs, facilities, and financial assets, and employing those resources to equitably leverage the greatest possible benefit for the Citizens of the City of Durham.

The following events are highlights of the 2000 – 2001 fiscal year:

Reducing the incidence of crime and root causes of crime. The City's crime numbers dropped in calendar year 2000, maintaining a two-year trend of steadily decreasing crime. Overall reported crime dropped 7% from 17,709 victims in 1999 to 16,394 victims in 2000. These numbers represent a 9% decrease in violent crime and a 7% decrease in property crimes. In 2000, City's overall crime rate per 100,000 residents was down 9% from 1999 and down 13% from 1998. In addition, a comparison with other North Carolina cities over 150,000 showed that Durham led all other major North Carolina cities in the percentage drop in crime in CY 2000 compared to CY 1999.

Youth Programming. In order to address the needs of the City's youth, the Parks and Recreation Department continued to offer teen programs through the athletics division and the recreation centers. The Department offered activities such as the Rites of Passage Program at four recreation centers, free teen night events, and computer literacy programs. Also, in the face of cutbacks in Federal funding for summer youth employment, the Office of Economic and Employment Development has strived to maintain or increase the number of 14 to 21 year olds that gain valuable summer work experience.

Employment & Training Incentive Funds. The City was awarded additional State employment and training incentive funds for exceeding established goals in five out of six areas. The incentive funds are used to help with both administrative and programming needs, which are vital at a time when fewer federal dollars are available for employment and training programs.

Ensuring the availability of, and access to, adequate, safe, and affordable housing for every resident.

HOPE VI Activity. In August 2000, the Housing Authority of the City of Durham (DHA) received a \$35 million HOPE VI grant from the U. S. Department of Housing and Urban Development for the revitalization of the Few Gardens neighborhood. The revitalization strategy includes:

- Building a variety of high-quality public, rental, and home ownership options attractive to a variety of income groups;
- Taking advantage of the area's proximity to downtown Durham, NC 147, and social service providers to appeal to different consumer groups;
- Providing community services that enable and encourage public housing residents to fully participate in and contribute their neighborhood;
- Create visually appealing edges and gateways by developing home ownership and privately managed rental units along border streets (Liberty Street, Maple Street, Elizabeth Street, and NC 147).

The HOPE VI revitalization strategy addresses the structural, design and site deficiencies of Few Gardens by replacing the 240 severely distressed units currently on the site with 160 high quality rental apartments and homeownership units. The impact of the revitalization project will then be expanded to the adjacent community with the redevelopment of 275 parcels along the major streets leading to or surrounding Few Gardens. Upon completion, the HOPE VI grant will develop 160 public housing rental units, 88 tax credit/affordable and market rate homeownership units, providing housing for 390 families. Displaced residents who meet program requirements will be given vouchers to subsidize their rents in privately owned apartments.

In addition to the HOPE VI grant, the revitalization plan relies upon \$30.3 million in equity leveraged through the use of Low Income Housing Tax Credits, \$20.7 million in City and County support, and \$15.2 million in leveraged Community and Supportive Services (CSS) programs. The City funds are targeted at road and street improvements, infrastructure upgrades, the development of parks and recreational facilities, homeownership programs, assistance with displacement of families, and a regular police presence at Few Gardens. Funds leveraged for CSS programs will support a range of education, employment, relocation, and family self-sufficiency services.

Providing economic development activities that increase citizen access to high quality jobs while increasing the City's tax base.

In August 1999, the City Council established the current Economic Development Investment Fund. It allows for reinvestment of capital investments when at least \$500,000 is invested within nine designated Community Development areas, located in and near downtown. In January 2000, the City Council adopted a companion policy to the Economic Development Investment Fund called the Job Creation Incentive Policy. This policy provides incentives of up to \$2,500 per job to be offered strictly on the basis of new job creation in the same designated area as the Economic Development Investment Fund. To be eligible for this incentive, a business must create at least 25 new, full-time, permanent jobs within two years of an agreement with the City.

In FY 2000-2001, the City Council approved the use of economic development investment funds for two projects:

- Valcor Inc. – Valcor Inc., a Raleigh-based contract electronic assembly-manufacturing firm, will renovate the historic International Paper industrial complex at 923 Franklin Street. The firm will invest \$600,000 in site renovations, and installation of new machinery. The company will move from Raleigh to Durham and create at least twenty-five new jobs at or

above the City's minimum wage standard. The \$36,000 payment is contingent on meeting job creation criteria within three years.

- Foster Street Partners - The City Council authorized up to \$60,000 reimbursement for the renovation of the 1934 Clark and Sorrell building at 323 Foster Street by the Foster Street Partners. The reimbursement will be made over two years and is contingent on capital investment by the owners of at least \$1,750,000.

Managing the City's growth, protecting and preserving the environment, and maximizing the use of public infrastructure

Implementation of Automated Collection System. In May 2001, the City introduced automated collections to over 9,000 Durham residents. Automated collection is a technologically advanced waste collection system employing a specially fitted refuse vehicle. Refuse is mechanically dumped into the truck from a curbside location. The operator uses a set of controls inside the truck cab to operate a mechanical arm that lifts, dumps and returns the container to the curb. The standard 90-gallon container is currently being serviced by semi-automated vehicles and is ideal for the fully automated vehicle.

The automated refuse collection vehicle has several advantages over traditional waste collection methods. An automated vehicle can do the same work as a conventional rear loader semi-automated vehicle while using only one operator. It is not anticipated that every semi-automated route can be replaced with a fully automated route. However, by eliminating semi-automated vehicles where practical, staffing levels can be lowered while increasing productivity and reducing job-related injuries.

The net annual savings per collection crew converted from semi-automated refuse collection to automated refuse collection is \$75,000. In the first three years of implementation, we will convert eight rear loader crews to eight automated crews, cutting 16 positions. This action saves salary and benefit costs of \$1 million over the next three years. Another six crews will be converted in FY 2004-05 and FY 2005-06, to provide for an accumulated cost avoidance of \$3 million in a five-year period. Based on current dollars, this system saves \$1 million every year after the fifth year of implementation when compared to the current semi-automated service (exclusive of costs associated with merit and employee benefit increases.)

Water and Sewer Fund Analysis. In February 2001 the City Council adopted a resolution that set financial standards for the Water and Sewer Fund. These standards include: a recommended level of retained earnings, minimum parity debt ratios, requires a mixture of pay as you go and debt financing, and standard for the appropriate use of retained earnings in the water and sewer fund.

For the Future

The major features of the FY 2001-02 budget include:

Revaluation - Durham County has completed the process of reappraising all real estate properties in the County to comply with the State requirement for general reappraisals (revaluation) every

eight years. The purpose of revaluation is to eliminate inequities that may have developed as a result of market value fluctuations. The revaluation brings all properties to a market value equivalent assessment as of January 1, 2001. Before the revaluation, all real properties were assessed at their 1993 market equivalent values. The revaluation will be in effect for tax bills due for FY 2001-02. These tax bills have been mailed to property owners and are due before January 5, 2002.

The Tax Assessor estimates the new real estate value to be \$12.3 billion, which represents an increase of 50%. The County projects that the Board of Equalization may reduce assessments by \$528 million through the appeals process. After Board of Equalization adjustments the real estate value will be approximately \$11.7 billion, which is an increase of 44%. Based on this information, the tax equalization rate for the City is 51.7 cents, compared to 69 cents prior to the revaluation.

Increased debt service requirements. In 1996, City voters approved a bond referendum totaling \$86 million for infrastructure improvements. At the time of the bond referendum the Administration projected that a tax increase of one cent per year would be needed to pay for the increased debt service. To this point, the City absorbed the increased debt service without increasing taxes. This year, the amount of debt service related to the issuance of the 1996 bonds has increased by over \$2 million, the equivalent of 1.62 cents on the new tax rate.

Maintenance Initiative. The City has numerous facilities that have not been adequately maintained to ensure their maximum useful life. Due to prior budget constraints, the scheduled maintenance for major systems, including roofs, HVAC, electric, plumbing, and structural, has not been fully funded. When items such as these are allowed to deteriorate, the repair of these facilities become major capital projects. A primary focus of this initiative is the maintenance and replacement of major system components in the parks and recreation facilities. These funds will allow the City to resolve care of facility and system replacement issues before they become major projects.

Elimination of Internal Service Funds - The entity wide reporting component of the new reporting model as issued by the Governmental Accounting Standards Board, GASB 34, requires the City to report all activity as either Governmental Activities or Business-type activities. Under this new reporting model, internal service funds are reported as consolidated with governmental or business type activities. The FY 2001-02 budget has been prepared to facilitate implementation of the new reporting model by transferring all internal service activities currently reported in internal service funds to the City's General Fund with the exception of the Risk Retention Fund.

Payment from Duke University for Fire Services. The City and Duke University have reached an agreement concerning payment for fire protection services provided by the City to Duke University. Duke University has agreed to pay the City a minimum of \$300,000 annually for these services starting in the FY 2001-02.

Fire Apparatus Replacement Strategy. A regular replacement schedule of apparatus will be adopted to stabilize the City's annual appropriation for replacement of emergency apparatus in the Fire Department. The proposed schedule submitted for the FY 2001-02 budget replaces six

engines, one ladder truck and two ambulances over a six-year period. Suitable vehicles removed from front line status are placed in reserve for a period of up to five years. The expected life of an engine and ladder truck is approximately 10 and 15 years respectively on front line status and five years in reserve.

Public Housing Programming. The Parks and Recreation Department currently provides after-school programming at four public housing sites. A total of 200 children, an average of 50 children per site, benefit from after school programs at these sites. The Department also provides teen programs and summer camp programs at these four sites.

The Housing Authority of the City of Durham (DHA) has agreed to assume staffing of the after-school programs at public housing sites, while the Parks and Recreation Department will expand programming at the sites, such as increasing the number of children participating in the computer enrichment program. By having DHA assume operations at its sites, the Parks and Recreation Department can reallocate staff positions to other sites that serve at-risk children and teenagers, as well as senior citizens.

Homeownership Activities. The City will focus efforts on home purchase programs directed at City police officers and public school teachers. The City will continue to offer numerous programs to meet City Council's goal of promoting a wide range of affordable housing options in the City. These programs include second mortgage, minor repair, side-by-side rehabilitation, individual rehabilitation and development account programs. In addition, the City proposes to charge a loan origination fee to for-profit and non-profit developers for single-family and multi-family housing developments during the upcoming fiscal year to help provide funding for other affordable housing activities.

Housing Code Enforcement. In the upcoming year, the City will develop "targeted redevelopment strategy areas" to focus multiple resources to stabilize neighborhoods, promote homeownership and improve the quality of investor properties. This effort will be spearheaded by an aggressive code enforcement initiative. New mobile hand-held computers will allow inspectors to collect and research data in the field, which will lead to a direct increase in the amount of time spent performing code enforcement inspections. The vacant house database will be updated to allow the City to quantify progress in revitalizing these targeted areas by eliminating vacant structures from the housing stock through code enforcement or demolition. New fees are also proposed to reduce the number of reinspections performed by housing inspectors prior to property owners completing cited code violations and to act as an incentive for property owners to quickly meet all code enforcement requirements. Multiple reinspections on a single property prevent code enforcement staff from increasing the numbers of units brought into compliance annually.

Lead-based Paint Abatement. The U.S. Department of Housing and Urban Development (HUD) has awarded federal funds to the City to mitigate lead-based paint in housing and to educate the community on lead paint issues. The grant, which totals over \$2.4 million, will be used in the upcoming year to address lead-based paint hazards in approximately 105 homes in conjunction with the City's existing rehabilitation program. Funds will also be used to conduct a citywide educational campaign, train housing inspectors and housing rehabilitation contractors in

lead awareness and abatement methods, and to teach up to 70 individuals lead hazard job skills, ultimately qualifying them for lead abatement program certifications.

Downtown Revitalization Activities. In the coming year, the City will lay the groundwork for additional private-sector investment in the downtown area by:

- Implementing downtown street conversion projects, as called for in the Downtown Master Plan;
- Providing for the redevelopment of the Woolworth property, a prime downtown location on Parrish and Main Streets;
- Providing for a redevelopment and beautification plan for the Parrish Street area, and,
- Working with the owners of the Liggett & Myers and American Tobacco campuses to realize the renovation of those key properties.

Small Business & Technology Development Center. The City in cooperation with North Carolina Central University and other local economic development organizations will provide funding for the Small Business and Technology Development Center (SBTDC) to increase its presence in Durham. The Center will also provide "pre-venture" services to more than 100 individuals contemplating new business start-ups. The SBTDC focuses 65% or more of its efforts on work with existing small businesses, where 70% or more of new jobs historically are created to help take these companies to their "next level" of growth and prosperity. As a result of this strategic focus, the SBTDC is non-duplicative of the organizations in the community that have a primary focus on "start-ups".

Stormwater Non-Infrastructure Expenses. In the FY 2001-02 budget storm water non-infrastructure expenses are moved from the General Fund to the Stormwater Fund. Stormwater non-infrastructure covers storm water quality management activities such as industrial inspections, public education and illegal disposal. This change in funding source is due to recently adopted enabling authority from the N.C. General Assembly. The total cost for the stormwater non-infrastructure program is approximately \$465,000.

Grants and Loans Financial Compliance Initiative. For the past several years, the City has made a concerted effort to receive more grants and make loans to citizens and new and/or small businesses. As a result, the City has numerous departments initiating grant applications, drawing grants funds and making loans. Therefore the acceptance, financial monitoring and draw down of grant funds and loans have been inconsistent. This has resulted in significant delays in receiving grant drawdowns. The general fund, which is providing cash to grant programs, has maintained a receivable from grants of between \$2 and \$4 million. This excess grants receivable amount depresses amount of the year-end general fund undesignated fund balance and overall interest earnings. The FY 2001-02 budget establishes a financial compliance division that will coordinate the financial compliance components of grants and loans for the City.

Risk Management. The City has begun several initiatives designed to prevent losses and improve claims handling. These include the hiring of third party independent claims adjusters, the use of a medical bill review service for worker's compensation claims and periodic claims auditing by an independent third party. In addition, the City has created a loss prevention

committee to coordinate efforts to reduce exposure to losses and to assist in the implementation and evaluate safety programs and safety training.

FINANCIAL INFORMATION

Accounting System and Budget Control

The diverse nature of governmental operations and the necessity of assuring legal compliance preclude recording and summarizing all governmental financial transactions and balances in a single accounting entity. From an accounting and financial management viewpoint, a governmental unit contains several different fiscal and accounting entities that function independently. Each accounting entity is accounted for in a separate “fund”. A fund is a self-balancing set of accounts recording cash and other financial resources together with related liabilities and residual equities or balance and changes therein. Each entity is segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions or limitations.

The various funds and account groups of the City have been classified into fund categories and types as follows:

Governmental	General, Special Revenue, Capital Projects
Proprietary	Enterprise, Internal Service
Fiduciary	Trust and Pension Trust
Account Groups	General Fixed Assets, and General Long-Term Obligations

The City’s accounting records for general governmental operations are reported on the modified accrual basis, whereby revenues are recognized when measurable and available and expenditures are recognized when goods and services are received. Accounting records for the City’s proprietary and pension trust operations are reported on the full accrual basis.

The City’s internal accounting controls are designed to provide reasonable, but not absolute, security of assets against loss from unauthorized use. The controls are also essential for sustaining the reliability of financial records for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that (1) the cost of control should not exceed the benefits likely to be derived; and (2) the evaluation of costs and benefits requires estimates and judgments by management.

As a recipient of Federal and State financial assistance, the City also is responsible for maintaining an adequate internal control structure to ensure compliance with laws and regulations related to those programs. As a part of the single audit, tests are made to determine the adequacy of the internal control structure and its compliance with applicable laws and regulations. The results of the City’s single audit for the fiscal year ended June 30, 2001 provided one instance of a significant violation of applicable laws and regulations. There were five minor instances of reportable conditions in the internal controls structure. The City has implemented processes to correct any weaknesses in the internal controls structure.

Budgetary controls are maintained to ensure compliance with the budget as adopted or amended by City Council. The North Carolina General Statutes require the adoption of an annual budget for all funds except those for which expenditures are authorized by project ordinance, fiduciary funds and internal services. In those instances a project ordinance or financial plan is adopted by the City Council. The City Manager has the authority to transfer budgeted amounts between departments within any category. However any revisions that alter the total appropriations of any category or fund must be approved by the City Council.

Encumbrance accounting under which purchase orders, contracts and other commitments for the expenditure of monies are recorded in order to reserve that portion of the applicable appropriation is employed in all governmental funds. Encumbrances outstanding at year-end are reported as reservations of fund balance. Funds to cover outstanding encumbrances are reappropriated through the budgetary process.

General Government Functions

Revenues for general governmental function (General, Special Revenue and Capital Projects Funds) amounted to \$148,156,380 for the fiscal year ended June 30, 2001. Below is a comparative summary of General Fund revenues from various sources:

	Fiscal Year Ended June 30, 2001	Fiscal Year Ended June 30, 2000	Increase/ (Decrease)	Percent Increase/ (Decrease)
Taxes	\$94,030,267	\$88,865,017	\$5,165,250	5.8%
Licenses and permits	6,482,505	5,100,928	1,381,577	27.1%
Intergovernmental revenues	17,250,240	15,968,499	1,281,741	8.0%
Investment and rental income	2,885,734	1,802,279	1,083,455	60.1%
Charges for services	7,579,509	7,840,699	(261,190)	(3.3%)
Intragovernmental services	301,432	1,534,612	(1,233,180)	(80.4%)
Assessments	354,308	204,743	\$149,565	73.1%
Sale of property and miscellaneous	634,317	348,605	\$285,712	82.0%
Total	\$129,518,312	\$121,665,382	\$7,852,930	

Total General Fund revenues increased by 6.5%. Tax revenues, which represented 72.6% of the total General Fund revenues for FY 2000-01 increased by 5.8%. The reason for the increase is

the growth in the City's tax base, a one-penny increase in the tax rate and an increase in sales tax revenues. The property tax rate increased from .68 cents (per \$100 of assessed value) in FY 2000 to .69 cents (per \$100 of assessed value) in FY 2001. The increase in tax revenues occurred despite a decline in rate of tax collections from 95.4% to 95.3%. The large increase in investment and rental income was due to the adjustment to fair market value of various investments held by the city. The large decrease in Intragovernmental services is due to the delay of the Intangibles tax reimbursement from state of North Carolina. This revenue was delayed by the state due to budget constraints and was received in October 2001, which was too late to be included in fiscal year 2000-2001 revenues.

Expenditures for general governmental function (General, Special Revenue and Capital Projects Funds) amounted to \$163,030,692 for the fiscal year ended June 30, 2001. Below is a comparative summary of General Fund expenditures from various sources:

	Fiscal Year Ended June 30, 2001	Fiscal Year Ended June 30, 2000	Percent Increase/ Decrease	Percent Increase/ Decrease
Governance	\$4,250,583	\$5,101,193	(\$850,610)	(16.67%)
Public Protection	52,968,210	50,662,297	2,305,913	4.55%
Community Services & Development	43,334,824	36,282,633	7,052,191	19.44%
Administrative and Support Services	3,719,618	3,270,245	449,373	13.74%
Nondepartmental/Miscellaneous	6,450,641	8,179,360	(1,728,719)	(21.14%)
Debt Service	<u>10,674,979</u>	<u>9,658,463</u>	<u>1,016,516</u>	10.52%
Total	\$121,398,855	\$113,154,191	\$8,244,664	

Expenditures in the General Fund increased by 6.8%. Most of this increase was due to salary increases and community development initiatives. Changes in the distribution of expenditures due in large part to the reassignment of departments and activities to different functional categories

Fund Balance in the General Fund

The fund balance in the General Fund decreased from \$27.8 million in FY 2000 to \$27.6 million in FY 2001. The FY 2001 undesignated fund balance is \$13.3 million, which is a 5% decrease from the prior year. This decrease of the undesignated fund balance is due to increased amounts reserved by state statute, specifically amounts due from other funds where the General Fund provided advances for expenditures that are reimbursable by grants. The amount due to the General Fund from other funds, due to advances for reimbursable grants, was \$ 3.1 million as of 6/30/2001. This amount should be significantly lower. The failure to draw-down grant funds on a timely basis inflated the amount due to the General Fund. The City Council has adopted a policy of maintaining an undesignated fund balance of no less than 12% of budgeted appropriations, adjusted for debt service and transfers to other funds. The FY 2001 undesignated fund balance is 10.6% of FY 2002 budgeted appropriations adjusted for debt service and transfers to other funds. In preparation for the implementation of GASB 34, the City closed most of the Internal Services Fund at the end of FY 2001. The close of the Internal Service Funds into the General Fund at June 30, 2001 increased the appropriations in the General Fund, which lowered the percentage of fund balance in proportion to total appropriations. With out the added

appropriations from internal service funds the amount available would have been approximately 12.5% of budget appropriations for FY 2001-02.

Proprietary Activities

There are eight separate proprietary activities accounted for in the City's enterprise funds: Water and Sewer, Stormwater, Ballpark, Transit, Parking, Parking Control, Solid Waste Disposal, and Civic Center. The Water and Sewer Fund had equity of \$117,441,901 as of June 30, 2001 compared to \$108,896,918 for June 30, 2000. The Water and Sewer Fund had a net gain of \$6,186,481 compared to a net loss for the year ended June 30, 2000 of \$823,098. This change is due to an adjustment of depreciation schedules. Last year depreciation expense was \$13,612,267. After the adjustment the depreciation for the water and sewer fund is \$6,922,787 or a decrease of \$6,689,480.

In previous years, the City depreciated buildings over a 25 - 27 year useful life and land improvements over a 35 year period. This schedule did not reflect the true economic life of the assets and has been changed to more accurately reflect the true cost of depreciation. The new depreciation schedule uses a useful life of 40 years for buildings and a 50 year life for land improvements. This change reduces depreciation charges for this year and subsequent years. A complete depreciation schedule used by the City can be found in the Notes to the Financial Statements.

The Water and Sewer, Stormwater Management and Solid Waste Fund are operated without subsidy from the City's General Fund. The remaining Enterprise Funds received operating transfers from the General Fund as follows:

- Parking Facilities Fund \$1,224,053
- Transit Fund \$3,399,890
- Civic Center Fund \$231,304
- Ballpark Fund \$1,303,351

The City's Internal Service Funds account for the following functions: Asset Management, Cash Management, Central Radio Lease, Employees' Health Benefits, Centralized Fleet, Information Systems and Risk Retention. Services provided by these functions are billed to users on the basis of estimated costs of operations. Except for the Risk Retention Fund, all Internal Service Funds are being transferred into the General Fund at the end of FY 2001.

Fiduciary Operations

The City's Fiduciary Funds account for resources held by the City as trustee for which the City acts as the agent. The amounts for which the City provided custodial responsibilities following:

Cemetery Perpetual Care	\$1,749,807
Transit Trust	9,716,775
Law Enforcement Officers Separation Allowance	<u>2,398,727</u>
Total	\$13,865,309

Pension Trust Fund Operations:

Under a mandate from the North Carolina General Assembly, the City began funding the Law Enforcement Officers Separation Allowance in 1987. An actuarial study conducted as of December 31, 2000, in accordance GASB No. 27 showed a pension benefit obligation of \$7,025,893. Through June 30, 2001, the City had funded 31.5% of that total.

Debt Management

The City's sound financial condition is evidenced by the maintenance of AAA/Aaa bond ratings for general obligation debt from Moody's, Standard and Poors and Fitch IBCA. The City is one of the few municipalities to receive the highest general obligation bond ratings from the three rating agencies. The City's credit ratings for general obligation and water and sewer revenue debt are listed below:

	Standard & Poor's	Fitch IBCA	Moody's
General Obligation	AAA	AAA	Aaa
Water and Sewer System Revenue Bonds	AA	AAA	Aa3

These strong credit ratings allow the City to issue debt at interest rates considerably below the Bond Buyer's Index, thereby achieving significant savings.

As of June 30, 2001, the City had debt outstanding of \$363,755,810 compared to the previous fiscal year total of \$364,849,758. The total debt outstanding consists of \$219,520,000 outstanding general obligation bonds, \$28,095,000 in revenue bonds primarily for the expansion and improvements to the city's water and sewer system, \$32,331,493 due to Durham County for purchase and improvements to sewer lines, \$9,750,000 in a loan from the state to improve a sewer treatment plant and \$68,470,000 in certificates of participation.

Bonds authorized but unissued at June 30, 2001 were \$52,682,000 consisting of:

Art and Museum	\$ 326,000
Housing	\$ 12,525,000
Park & recreational facility	\$ 9,103,000
Public Transportation	\$ 5,165,000
Streets	\$ 25,563,000
Total	\$ 52,682,000

Cash Management

Effective forecasting of cash requirements and progressive cash management has allowed the maximum use of all available cash resources. For the year ended June 30, 2001, the City's Gross investment income was \$10,267,098, which is an adjusted increase of \$2,480,044 from the previous fiscal year. This amount includes a GASB Statement 31 market value increase in the amount of \$3,247,148. This increase represents a one-time adjustment to the investment portfolio. The City's average weighted yield to maturity for the pooled cash at June 30, 2001, was 5.29%.

The City uses the pooled cash and investment concept in investing excess cash for all funds. The goal of the City's investment policy is to minimize credit and market risk while receiving high returns on investments. The investment policy of the City is guided by NCGS 159-30, which

stipulates that the City can only invest in certificates of deposit, repurchase agreements, secured time deposits, banker's acceptances, commercial paper, and United States government and agency securities.

General Fixed Assets

The general fixed assets of the City are those fixed assets used in the performance of general governmental functions and exclude the fixed assets of proprietary funds. As of June 30, 2001, the general fixed assets of the City amounted to \$242,900,310. Depreciation of general fixed assets is not required.

Risk Management

The City has established Risk Management programs to (1) identify potential exposure to loss, (2) evaluate the frequency and severity of losses, (3) determine the most efficient use of financial resources to pay for losses that are not preventive, (4) reduces or eliminates risks or losses through procedures and practices. Additional information relative to insurance coverage and risk retention is presented in the Notes to the financial statements.

OTHER INFORMATION

Independent Audit

State Statutes require an annual audit by independent certified public accountants. The accounting firm of Cherry, Bekaert & Holland was selected by the City Council. In addition to meeting statutory requirements, the audit also complies with the Federal Single Audit Act, Office of Management and Budget Circular A-133, and NCGS 159-34 (Single Audit Implementation Act). The auditors' report on the general-purpose financial statements and combining and individual fund statements and schedules are included in the financial section of this report. The auditors' reports on internal controls and compliance with applicable laws and regulations are included in the Single Audit Section.

Award

The Government Finance Officers Association of the United States and Canada (GFOA) once again recognized the City for the quality of its Comprehensive Annual Financial Report issued for the previous fiscal year. In order to be awarded a Certificate of Achievement, the City must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and accepted legal requirements. This Certificate of Achievement for Excellence in Financial Reporting marks the 16th consecutive year and the 20th time in 22 years that the City has been so honored.

A Certificate of Achievement is valid for a period of one year only. We believe that our current report continues to conform to the Certificate of Achievement Program requirements, and we are submitting the report to GFOA to determine its eligibility for another certificate.

Acknowledgments

Preparation of this report would have been impossible without the hard work and dedication of the Department of Finance Staff. In particular the efforts of the Accounting Staff and the

Financial Reporting Team should be recognized. Other departments of the City have also contributed directly or indirectly in the preparation of this report and their cooperation and continued assistance is appreciated.

We also greatly appreciate the ongoing support and guidance we receive from the Mayor and the City Council.

Respectfully submitted,

Marcia L. Conner
City Manager

Navdeep S. Gill
Director of Finance